

Message Text

SECRET

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ACTION EUR-12

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S E C R E T LISBON 0621

PASS TREASURY FOR YEO AND SYVRUD

E.O. 11652: GDS
TAGS: EFIN, ECON, PO
SUBJ: FINANCIAL ASSISTANCE TO PORTUGAL

REF: (A) LISBON 0573, (B) LISBON 0499, (C) LISBON 0587

1. AT CLOSE OF CONVERSATION REPORTED REFTEL (A), I
ASKED FINANCE MINISTER MEDINA CARREIRA TO CONVEY THE
ESSENCE OF OUR POSITION TO PRIME MINISTER SOARES,
BECAUSE I HAD FRANKLY BEEN A BIT PERPLEXED BY SOARES'
INTERVENTION REPORTED REFTEL (B). AS A RESULT, SOARES
TELEPHONED ME TODAY AND ASKED ME TO COME AROUND FOR
ANOTHER DISCUSSION.

2. I EMPHASIZED TO SOARES THE IMPORTANCE OF PROCEEDING
RAPIDLY WITH THE LOAN ALONG THE LINES THAT HAD BEEN
NEGOTIATED. OTHERWISE, CONGRESSIONAL APPROVAL
OF CONSORTIUM COULD BE PUT IN JEOPARDY.

3. SOARES SAID HE HAD NO INTENTION OF TRYING TO REOPEN
NEGOTIATIONS ON THE \$300 MILLION. HE HAD SIMPLY FELT
OBLIGED TO POINT OUT TO USG THE DELICATE POLITICAL
SITUATION IN WHICH THE SOCIALIST GOVERNMENT FOUND ITSELF
AND THE IMPACT THAT THE LOAN WOULD HAVE ON THE INTERNAL
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POLITICAL SCENE. THE SOCIALISTS, HE SAID, WERE UNDER
HEAVY ATTACK FROM THE COMMUNISTS, THE FAR RIGHT AND NOW
THE PPD/PSD. THEY FULLY INTENDED TO TAKE THE MEASURES
NECESSARY TO GET THE ECONOMY BACK ON COURSE, BUT THESE
MEASURES WOULD INEVITABLY CAUSE SOCIAL DISLOCATION. IF
THEY WERE NOT PROPERLY HANDLED THEY COULD RESULT IN THE
GOVERNMENT'S DOWNFALL.

4. SOARES SAID IT WAS IMPORTANT THAT THE GOP BE PERCEIVED TO BE TAKING THESE MEASURES ON ITS OWN AND NOT UNDER PRESSURE FROM THE USG. THIS WAS PARTICULARLY TRUE SINCE DELICATE BUSINESS ISSUES SUCH AS ITT WERE COMING TO A HEAD AT THE SAME TIME AS THE LOAN NEGOTIATIONS. HE COULD ACCEPT THAT DEVALUATION WAS NECESSARY, BUT THE TIMING AND AMOUNT OF THE DEVALUATION HAD TO BE GAUGED CAREFULLY. A LARGE DEVALUATION LINKED TO THE AMERICAN LOAN COULD VERY WELL PROVE FATAL FOR THE GOVERNMENT.

5. I REPEATED TO SOARES THE LEGAL CONSTRAINTS ON THE USE OF THE EXCHANGE STABILIZATION FUND, AND NOTED THAT HE HAD ALWAYS AGREED THAT THE GOP WOULD HAVE TO BECOME ENGAGED WITH THE IMF. THE QUESTIONS OF TIMING AND AMOUNT OF THE DEVALUATION WERE ITEMS TO BE NEGOTIATED, AND FRANKLY THE GOP HAD NOT BEEN NEGOTIATING WITH THE IMF AS WELL AS IT COULD HAVE. PROPERLY HANDLED, THERE WOULD BE NO NEED TO ASSOCIATE A DEVALUATION WITH THE USG LOAN. ONE OF THE PURPOSES OF GIVING THE GOP FOUR (NOW FIVE) OPTIONS WAS TO ALLOW THEM THE FLEXIBILITY TO DEAL WITH POLITICAL EXIGENCIES.

6. SOARES SAID HE UNDERSTOOD THIS AND RECOGNIZED THAT THE GOP HAD TO DEAL WITH THE IMF. HOWEVER, HE COUNTED HEAVILY UPON THE UNDERSTANDING OF THE USG AND ITS HELP TO AVOID CONDITIONS THAT MIGHT BE POLITICALLY UNREALISTIC. AFTER ALL, WE HAD FOLLOWED THE POLITICAL EVOLUTION HERE CLOSELY AND HAD RECOGNIZED THE PROGRESS THAT HAD BEEN MADE

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TO DATE. WE HAD ALSO TO BE AWARE THAT THE DANGER OF FALLING BACK INTO CHAOS WAS A REAL ONE IF THE ECONOMIC MEASURES WERE NOT PROPERLY TIMED AND IF THE USG LOAN COULD NOT BE EFFECTIVELY DEFENDED WHEN IT COMES BEFORE THE ASSEMBLY.

7. I ASSURED HIM THAT THE USG UNDERSTOOD THE PROBLEM AND THAT WE WERE TRYING TO BE AS HELPFUL AS WE COULD WITHIN OUR LEGAL CONSTRAINTS. I SUGGESTED THAT BEFORE WE TAKE ANY FURTHER ACTION WE AWAIT THE RESULTS OF THE GOP'S NEGOTIATIONS WITH THE IMF (REFTEL C) AND THE OUTCOME OF UNDERSECRETARY YEO'S CONVERSATION WITH THE BIS. I FELT CERTAIN THAT THE GOP WOULD FIND THE LOAN PROGRAM SATISFACTORY AS WE HAVE NEGOTIATED IT.

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